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CANADA-UNITED STATES TRADE NEGOTIATIONS: AN OVERVIEW

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Ministry of Treasury and Economics
Government of Ontario
May 1986

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SUMMARY

I. THE NEGOTIATING ENVIRONMENT

The U.S. merchandise trade deficit stands at over $124 billion. Canada can expect a tough bargaining posture by the Americans in the bilateral trade negotiations. Therefore, it will be important for Canada, at the outset of the discussions, to establish a number of key facts about the relative economic performance of the two countries and their abilities to accommodate further adjustment.

- The U.S. trade deficit is not a result of American trade policy.
- Structural change is more pronounced in Canada.
- Canadian unemployment is persistently higher.
- Canada's federal deficit is relatively higher.

II. THE IMPORTANCE OF SECURE ACCESS

Trade policy is much more important to Canada than to the United States. Some 31 percent of Canadian Gross National Product is earned through exports, while imports account for 32 percent of Gross National Expenditure. This compares to 9 per cent and 11 per cent respectively in the United States.

The U.S. is Canada's most important trading partner. Ontario's dependence on the U.S. market is even more pronounced.

The effects of American and Canadian contingency protection measures are not symmetrical. U.S. actions can shut Canadian exporters out of a relatively much more important market. Our exports to the U.S. account for 20.5 per cent of GNP whereas U.S. exports to Canada represent only 1.2 per cent of U.S. income. On an industry basis, differences in the importance of exports are even more striking.

Secure access for Canada means that whatever access we have, or can negotiate, must not be threatened by new protectionist legislation. It also means that existing trade laws in the U.S. will not be used to harass Canadian exporters and otherwise raise the cost and uncertainty of investing in, or exporting from, a Canadian location.

III. THE IMPORTANCE OF ENHANCED ACCESS

It is important that Canada convey to the United States the message that while there are potential benefits to Canada from free trade, these are by no means assured.

Wider markets and greater competition could lead to industrial rationalization and a much-needed improvement in Canadian productivity. However, there are basic weaknesses in the competitive position of many Canadian firms. These weaknesses are evidenced by both the size, and the persistence, of the **Canada-U.S. productivity gap.**

On average, Canadian manufacturing firms continue to be about 20 per cent less efficient than their American counterparts.

Major structural weaknesses among Canadian firms include:

- Suboptimal plant scale.
- Suboptimal product runs.
- Suboptimal firm size.
- Low R&D.
- Slow diffusion of technology.
- High Debt/Equity Ratios.

Canada's current competitiveness is largely a result of the depreciation of the Canadian dollar since 1976; it does not reflect underlying economic strength, or an ability to close the real income gap.

The Auto Pact stands as a model, not of free trade, but of managed trade.

The enormous improvement of Canadian productivity in the auto industry in recent years was not exclusively related to the absence of tariff barriers under the Auto Pact.

The Auto Pact safeguards were undoubtedly essential for the protection of production and jobs in Canada as the North American industry rationalized its operations.

Another unique feature of the Canadian, and Ontario, economies is the high degree of **foreign ownership.**

The corporate structure of multinational firms dictates behaviour which is often different from that of purely national enterprises.

A wide range of corporate responses to free trade might be expected since not all multinationals are structured in the same way. But the uncertainty of these responses is important. Such considerations were held to be critical by the Government of Canada in 1965, when it insisted that production safeguards be included in the Auto Pact.

Services account for about 70 per cent of total Canadian employment.

Many Canadian service industries, including some business and professional services, experience competitive problems relating to small firm size, marketing capability and access to capital. The importance to the service sector of intangible capital, such as previous professional or business association and goodwill, implies that access may be particularly difficult for exporters in this sector.

The financial and insurance industries will become an important testing ground for the principles of "national treatment" and "right of establishment". Given the complexity of such principles, it would be preferable for Canada to negotiate service-related issues on an industry-by-industry basis.

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The larger **adjustment problem** for Canadian industries relates to Canada's greater trade dependency and the sizeable gap in Canadian relative productivity in certain areas. These factors suggest that Canada should pursue a long differential phase-in period, in which U.S. tariff and non-tariff barriers come down more rapidly than Canadian barriers.

Canadian owned firms may be differentially affected. Canada should avoid agreeing to "national treatment" rules that preclude special transitional support directed to Canadian-owned firms.

IV. WHAT BENEFITS? AT WHAT COST?

The prospect of achieving income and employment gains makes it worthwhile for Canada and the United States to explore options for improved trade. On the other hand, the estimated income gains in these models are not compellingly large compared to those available from other policy initiatives.

There is no evidence that bilateral free trade will:

- diminish the severity of business cycles;
- promote the goal of regional development;
- increase the diversification of our industrial structure; or
- significantly improve Canada's employment prospects.

Therefore, it is important that U.S. negotiators appreciate that Canada cannot relinquish its freedom to pursue independent economic policies to achieve these other goals.

Canada is comprised of 25.5 million residents. The United States has 240 million. Canadians occupy the second largest nation in the world, with the longest coastline. About 90 per cent of the Canadian population is located within 100 miles of the U.S. border.

In these circumstances it is critical that Canada not relinquish its right, or its flexibility, to support its **cultural industries.**

Regional development and income redistribution inevitably involve a cost which is borne by some Canadian taxpayers and some regions of Canada. As a consequence, where these policies might be seen to advantage some competitors, they clearly must disadvantage others in the same country. Americans must appreciate this reality, and respect the social and economic imperative of these policies.

The pricing of resources, for example oil, gas and electricity, is often used as a regional development policy. To constrain this tool of development is to undermine often the only viable opportunity for growth.

Agriculture is a special case in both Canada and the United States.

Any attempt to change the rules relating to agricultural trade will unleash major fiscal, economic and social dislocation. Both Canada and the United States must recognize the current poor timing of a major bilateral trade initiative in this

sector. However, general changes in contingent protection, as they affect agriculture, should be discussed.

Industrial policy takes different forms in different countries. In the United States, for example, industrial policy is closely linked to defence policy.

Since Canadian firms are frequently small by international standards, they are disadvantaged in world markets. **Industrial policy** is a way to offset these disadvantages and make the "playing field" within any industry more equal.

Any attempt to "fix" **the exchange rate** between the two countries would eliminate for Canada a powerful tool of international and domestic adjustment. It would deprive us of our ultimate protection should free trade turn out to have a strongly negative effect on the Canadian economy. It would be a price too large.

It is vital that the U.S. negotiators recognize the significant structural differences between the U.S. and Canadian economies. These structural differences may well require the use of different policy instruments to pursue even mutually held goals. The "level playing field" has to take into account the unique characteristics of industrial structure, geography, climate, population and culture of our two countries.

CHAPTER I. THE NEGOTIATING ENVIRONMENT

These are difficult times for the U.S. economy. The economic expansion has slowed. Projected cuts in the Budget deficit will produce considerable political and economic pain. The merchandise trade deficit stands at over $124 billion. The Congress is clearly angry with the Administration over what appears to them as passivity with respect to U.S. trade policy. As a result of all these pressures, Canada can expect a tough bargaining posture by the Americans in the bilateral trade negotiations.

In this context, it will be important for Canada, at the outset of the discussions, to establish a number of key facts about the relative economic performance of the two countries.

- The U.S. trade deficit is not a result of American trade policy, or evidence of a need to realign trade relationships. It is simply a reflection of U.S. macro-economic policy, the delayed recovery of Western Europe and the low import penetration of Japan. No matter how dramatic, the U.S. trade deficit is a cyclical economic problem.

- Both Canada and the United States are undergoing profound structural changes in their economies as fewer people are employed in the resource sectors and manufacturing, and more are employed in services. However, these changes have had a more severe impact in Canada. In the period 1981-1985, Canada lost 171,000 jobs in the manufacturing and resource sectors, 1.6 per cent of non-agricultural employment. U.S. job losses during 1981-1985 were only 0.7 per cent of non-agricultural employment.

- Structural dislocation has been accelerated by the collapse of commodity prices, continued high real interest rates and the high debt loads of business. Again, Canada has a more difficult situation to manage. Canadian long-term borrowing rates remain 150-200 basis points higher than in the U.S. U.S. non-financial corporations show debt-to-asset ratios of about 40 per cent compared to more than 60 per cent in Canada.

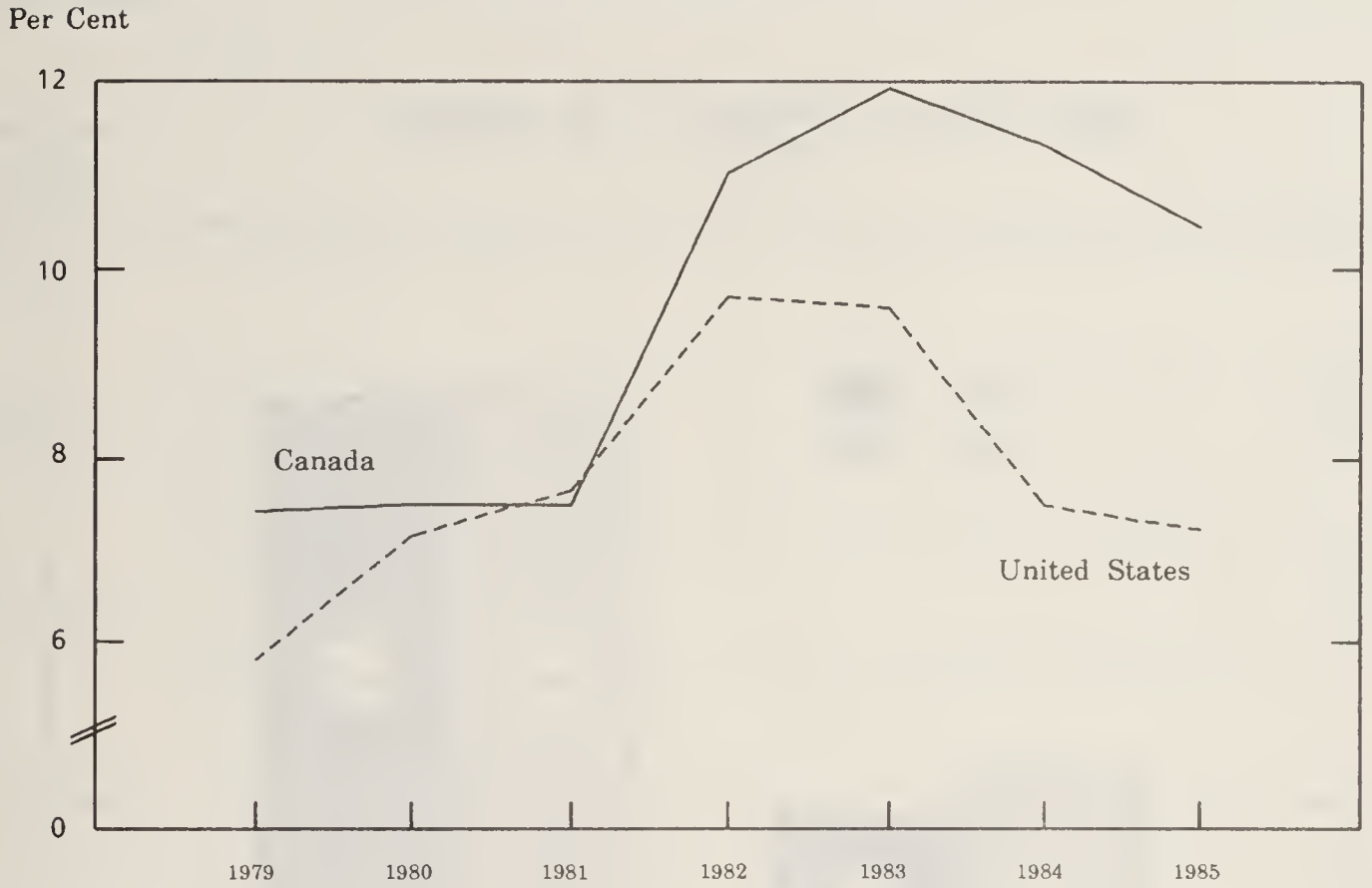
- The current low relative value of the Canadian dollar is a two-edged sword. It maintains the competitiveness of our exports. On the other hand, it increases the cost to Canadian firms of imported machinery and equipment. Compared to the United States, Canada imports much more of its machinery and other equipment. These additional costs, when coupled with higher real interest rates and a more levered financial structure, will slow down the necessary upgrading of the business capital stock.

- The difficulties of the resource industries have produced problems of regional adjustment in both countries. However, these problems are

more difficult to deal with in a small, open economy with limited diversity.

- The fundamental structural changes in the Canadian economy are taking place in the context of rapid labour force growth. The Canadian labour force will grow at 1.7 per cent per year from 1985 to 1990 while U.S. labour force growth is projected to be around 1.3 per cent. It will therefore be necessary to maintain higher employment growth in Canada than in the U.S. if Canada's unemployment problem is to be contained.

UNEMPLOYMENT RATES



Note: Drawn from Annual Averages

- Canada has experienced persistently higher unemployment than the U.S. in recent years. Even after three years of economic expansion in both countries, Canada has greater excess capacity. The Canadian unemployment rate stood at 9.6 per cent in March 1986 compared to 7.2 per cent in the U.S.

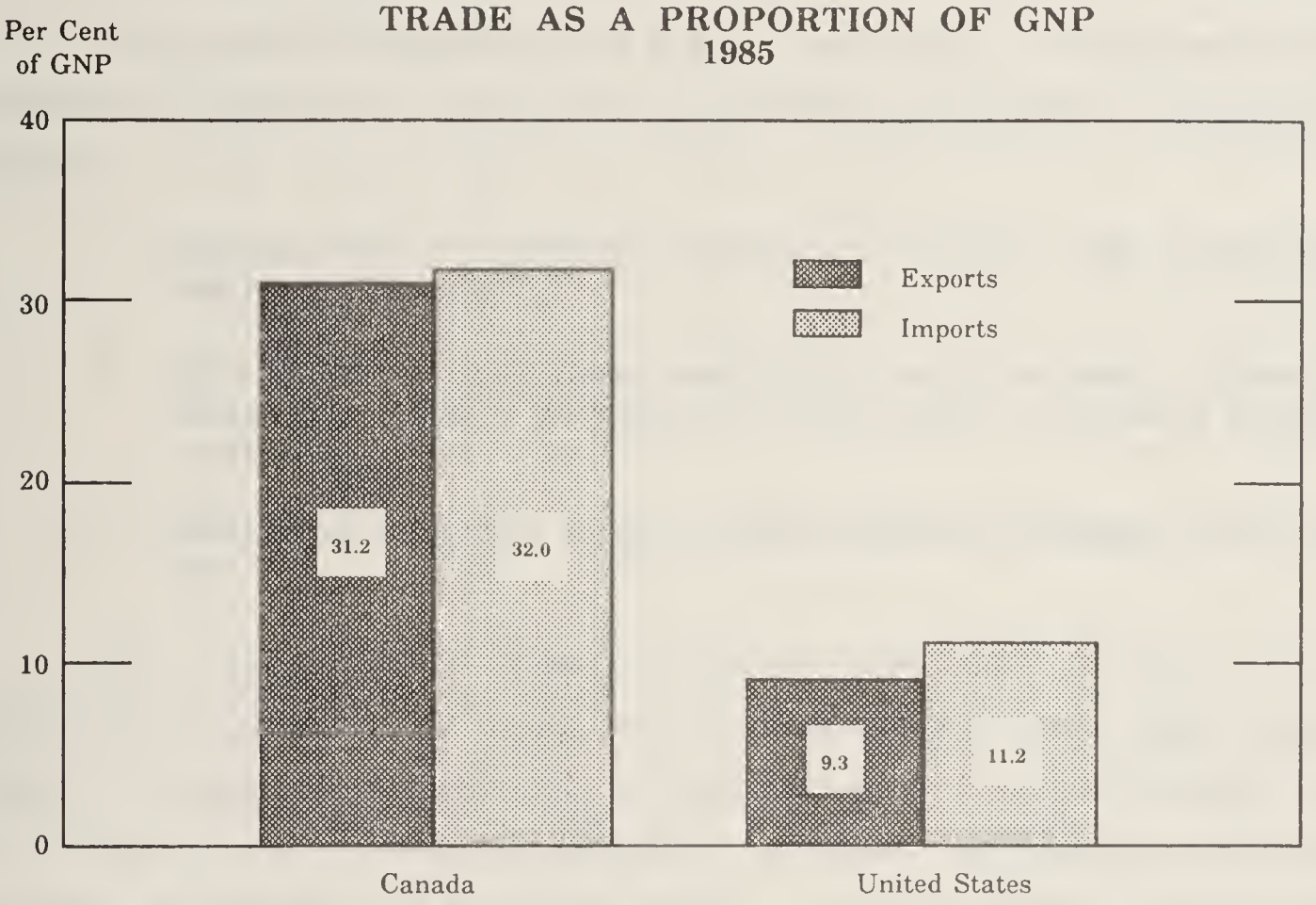
- The financial resources of the federal government in Canada to deal with employment dislocation are even more constrained than in the United States. The federal government's deficit in Canada is 7.1 per cent of GNP compared to 5.4 per cent in the United States.

These are all essential facts that need to be conveyed to the Americans.

CHAPTER II. THE IMPORTANCE OF SECURE ACCESS

Canada's Trade Dependency

As shown in the Chart, trade is much more important to Canada than to the United States.[1] Some 31 percent of Canadian Gross National Product is earned through exports, while imports account for 32 percent of Gross National Expenditure. This compares to 9 per cent and 11 per cent respectively in the United States.



While trade is critical to all of Canada, it looms even larger as a factor in Ontario's economy. The importance of trade to Ontario can be summarized in a few key facts:

- The province accounts for about 35 per cent of the Canadian population, and 38 per cent of gross domestic product, but generates 50 per cent of total merchandise exports and receives 63 per cent of total imports.

- Merchandise exports amount to about 34 per cent of total provincial product, making Ontario both absolutely and relatively the largest trading province in Canada.

1. See Appendices A and B for more detailed tables on trade flows and economic structure.

The U.S. is Canada's most important trading partner. Ontario's dependence on the U.S. market is even more striking:

- Ninety-one per cent of Ontario's merchandise exports are destined for the U.S., compared to 78 per cent nationally.
- Of the estimated 1.7 million Canadian jobs dependent on exports to the United States, one million are located in Ontario.
- About 83 per cent of Ontario's merchandise imports originate in the United States, compared to 65 per cent nationally. Ontario alone takes an estimated 14 per cent of U.S. merchandise exports to all countries.

The province's exports to the U.S. consist mainly of manufactured end products and fabricated materials. Autos and auto parts exports are especially important.

- Manufactured end products account for 73 per cent of Ontario's exports to the U.S.
- Fully 77 per cent of these exports are autos and parts. Thus, the automotive industry accounts for 56 per cent of Ontario's bilateral exports.
- Fabricated materials, such as lumber and steel, account for 22 per cent.

As a result of its diverse economic structure, Ontario will be significantly affected by all items on the comprehensive free trade agenda. Ontario is a manufacturing province, in 1984 accounting for an estimated 55 per cent of total Canadian manufacturing GDP. However, the province also has an important agricultural and resources sector. In 1984, Ontario accounted for almost 32 per cent of Canadian agricultural GDP (almost twice the share of Saskatchewan), 18 per cent of Canadian forestry GDP (only slightly less than B.C.'s share), and 15 per cent of Canadian mining GDP.

Ontario also has a large service sector, with strength in health, education, transportation, financial and business services. Employment in the service industries is almost 3 million people, or 68 per cent of Ontario's total employment.

The Meaning of Secure Access

The federal government has used the term "secure and enhanced access" to describe Canada's objectives in the bilateral trade negotiations. Clearly,

secure access is an important goal because of Canada's extreme dependence on the American market.

U.S. law provides for several forms of "contingent protection" or what Americans prefer to call "fair trade" or "trade remedy" measures.

- Countervailing duties may be imposed when an import is subsidized and causes material injury to a domestic industry such as reduced sales, profits or employment;

- Anti-dumping duties can be charged in instances where imports are priced at less than the "normal" prices charged in the exporter's domestic market and cause material injury to domestic industry in the United States;

- Safeguards, such as additional duties or quotas, can be imposed (temporarily) on fairly traded imports which nevertheless cause, or threaten, serious injury to domestic producers; and

- Retaliatory actions can be taken against exports of countries which are deemed to have unfair trading practices which restrict imports from the U.S.

Canada maintains equivalent forms of contingent protection. However, the effects of American and Canadian contingency measures are not symmetrical. U.S. actions can shut Canadian exporters out of a relatively much more important market. Canada's merchandise exports to the U.S. account for 78 per cent of total merchandise exports whereas U.S. exports to Canada account for only 22 per cent of their foreign trade. Our exports to the U.S. account for 20.5 per cent of GNP whereas U.S. exports to Canada represent only 1.2 per cent of U.S. income. On an industry basis, differences in the importance of exports are even more striking.

As indicated earlier, the U.S. currently has a trade deficit of $124 billion, the largest in its history. The result has been a large number of actual and threatened trade actions against non-American products, plus numerous bills to tighten and strengthen the application of U.S. trade laws. Specific actions have been launched against imports from Canada, notably lumber, hogs, potatoes and fish. A number of manufacturers, including producers of forklift arms, rectangular steel pipes and tubes, and commuter and business aircraft have had to spend significant financial and other resources in fending off threatened sanctions.

The increasingly aggressive enforcement of U.S. trade laws has important consequences for Canada. Even when Canadian products are not

impeded by contingency protection, the threat of legal action may add considerably to exporters' costs, or dissuade them from expanding their export efforts. In the longer run, if access to the U.S. is not reasonably certain, domestic and off-shore investors will find it increasingly attractive to establish new facilities within the United States, rather than Canada.

The United States must understand that wholly disproportionate sizes and vulnerabilities negate the "level playing field" concept in the general application of fair trade laws. Even the threat of protection has major trade and investment significance, although this issue is not addressed in the formal literature on the subject.

Secure access for Canada means that whatever access we have, or can negotiate, must not be threatened by <u>new</u> protectionist legislation. It also means that <u>existing</u> trade laws in the U.S. will not be used to harass Canadian exporters and otherwise raise the cost and uncertainty of investing in, or exporting from, a Canadian location. Particularly problematic is the application of countervailing duties.

Secure access need not entail the bilateral elimination of all contingent protection. In fact, complete elimination might unbalance existing trade arrangements in favour of the United States. For example, Canadian producers are vulnerable to U.S. dumping practices in the smaller Canadian market. They naturally rely on Canadian anti-dumping protection. Without resort to these remedies, Canadian firms could be left more exposed to dumped U.S. exports. Again, disproportionate size means that the excess capacity of U.S. producers would swamp the Canadian market.

Secure access does mean, however, that there will have to be at least <u>some</u> modification of American trade laws. There are numerous options that could be negotiated, including increased thresholds in injury tests relating to imports from the other country, anti-sideswipe provisions to exclude the signatories from safeguard actions directed at third countries, and introduction of a "balance-of-subsidies test" in order to ensure that only the subsidy differential is counted in determining the cause of an import-related injury.

If the United States accepts the general principle of secure access, then there are practical issues of how such a concept is negotiated. How can security of access to the U.S. market under any bilateral agreement be ensured, given the supremacy of Congress over U.S. trade legislation? Can a dispute mechanism be

established that gives Canada reasonable assurance that it will be accorded fair treatment? To what extent would a bilateral arrangement on contingency protection deprive the two countries of recourse to the appeal processes under the GATT?

Secure access is an important goal for Canada. But it is not a simple concept, and it will not easily be negotiated. It must involve some guarantees against future protectionist legislation. Equally important, however, it must involve some change to existing U.S. trade legislation.

CHAPTER III. THE IMPORTANCE OF ENHANCED ACCESS

Both Canada and the U.S. hope to achieve economic gains by reducing tariff and non-tariff barriers to trade. U.S. tariff barriers are important hurdles for Canadian exporters in certain sectors. Even more significant, a reduction in U.S. non-tariff barriers could yield important gains to Canada. For example, U.S. government procurement markets are highly protected by such instruments as the U.S. Surface Transportation Assistance Act and the Small and Minority Business Set Aside Program. Many Canadian exporters feel they could be successful in the procurement market were they not effectively excluded by this type of legislation.

It is important that Canada convey to the United States the message that while there are potential benefits to Canada from free trade, these are by no means assured. Bilateral free trade will create the opportunity for greater access to U.S. markets from Canadian locations. But Canada's ability to exploit this opportunity depends on the competitive positioning and the advantages and disadvantages of Canadian firms in each industry.

Secondly, free trade will expose Canadian firms to greater competitive discipline from competitors in U.S. locations. This discipline may act to improve productivity and make Canadian enterprises fully competitive with U.S. counterparts. But, again, whether this happens depends on the nature of competition in each industry and the relative competitive abilities of Canadian firms in those industries.

Wider markets and greater competition could lead to industrial rationalization and a much-needed improvement in Canadian productivity. However, there are basic weaknesses in the competitive position of many Canadian firms. These weaknesses are evidenced by both the size, and the persistence, of the Canada-U.S. productivity gap. As a result, it is a "leap of faith" to believe that Canadian firms will be able to adjust quickly to new export opportunities or new import competition.

Whether rationalization will actually occur -- and how smoothly it occurs -- depends critically on the content of any trade agreement. There are major risks:

- without adequate time and transitional industrial support policies, many domestic firms will be unable to restructure themselves to take advantage of new opportunities in the U.S.;

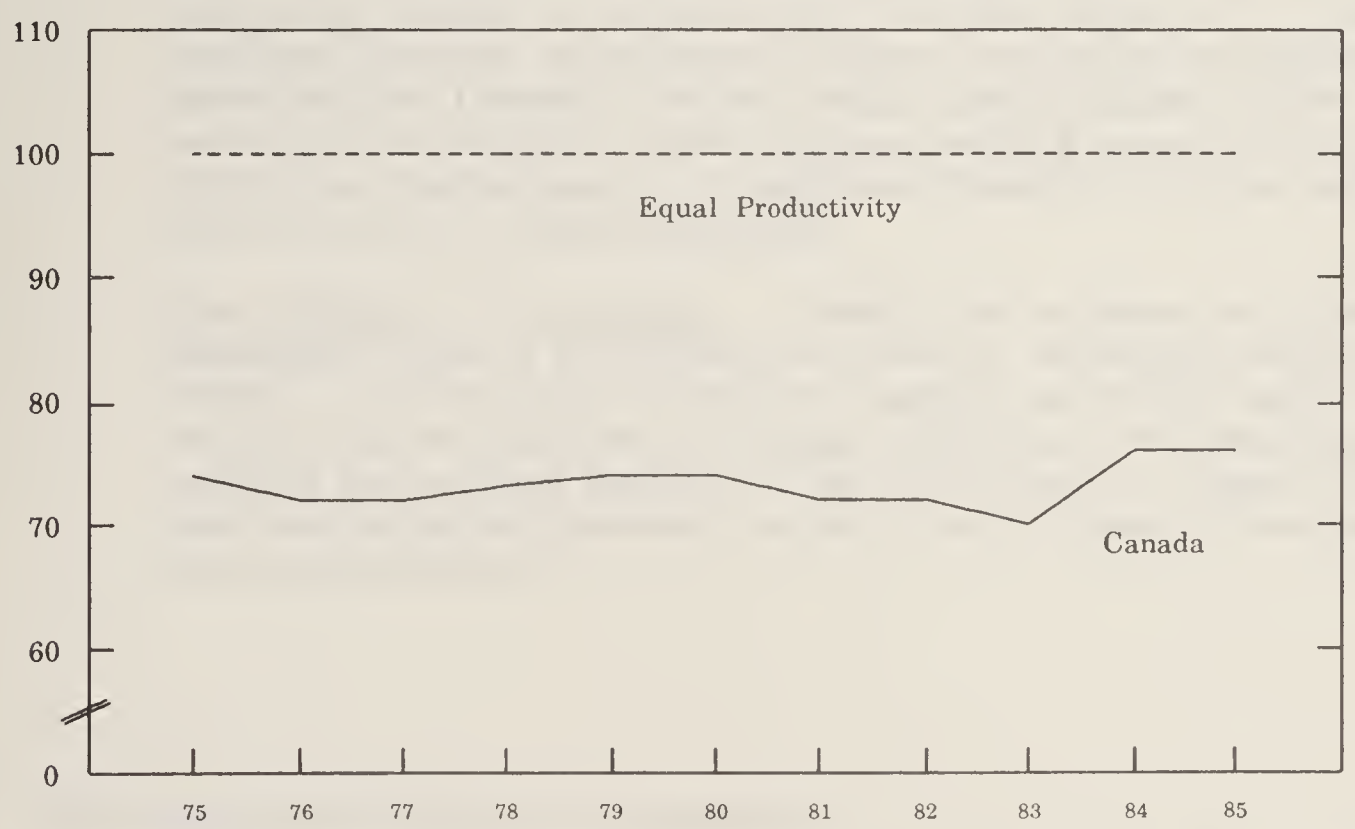
- with too abrupt a reduction in protection, uncompetitive firms that would ordinarily shrink over time will be forced into bankruptcy, with disruptive effects magnified throughout the economy; and

- without overall performance commitments, American multinational corporations might choose to locate all future investments in the U.S., and to supply Canadian markets through exports from their base in the United States.

An Enduring Productivity Gap

The size and persistence of Canada's manufacturing productivity gap relative to the U.S. is a dominant feature of its industrial structure. The productivity gap has remained essentially unchanged since the early 1970s. This is despite significant tariff reductions under the Kennedy and Tokyo rounds, and despite trade-induced rationalization along product lines. On average, Canadian firms continue to be about 20 per cent less efficient than their American counterparts.

CANADA'S PRODUCTIVITY GAP REMAINS SIGNIFICANT
(Canadian Productivity as a % of US)



Note: Productivity is Output Per Hour in Manufacturing.
Source: Data Resources Incorporated.

The dimensions and causes of this enduring productivity gap have been extensively explored in the Canadian literature on industrial organization and structure. Virtually hundreds of academic studies, indeed twenty years of

scholarly work on this subject, have repeatedly pointed to major structural weaknesses in Canadian firms.[1] Among the most prominent are:

- Suboptimal plant scale. Many Canadian plants are much smaller than their American counterparts. To cite one example, Baldwin and Gorecki concluded that about one-third of the productivity gap between Canadian and U.S. manufacturing sectors can be attributed to differences in plant scale between the two countries. They found that, in 1979, 99 out of 125 Canadian manufacturing industries examined possessed plants which were about half the size of those found in counterpart industries in the U.S.[2]

- Suboptimal product runs. Effective competition in many industries requires that Canadian firms produce a full range of products. This "miniature replica" effect entails short production runs and high change-over costs.

- Suboptimal firm size. Given the smaller and more dispersed Canadian market, Canadian firms typically experience relative diseconomies in distribution, marketing, finance, advertising and other central corporate functions.

- Low R&D. Canada's spending on R&D, relative to GNP, lags behind that in every major country, being 1.4 per cent here and about 2.7 per cent in the U.S. Canada's rapidly growing trade deficit in high technology products is noteworthy in this regard. A recent discussion paper by the Ministry of State for Science and Technology concluded that Canada is the only major industrialized country with trade deficits in all high technology commodity groups.[3] At the base of this poor performance is a weakness related to firm size and the predominance of foreign ownership.

- Slow diffusion of technology. Despite the reliance on imported technology, there is a relatively slow rate of technology diffusion in Canada. D. P. de Melto found, for example, an average lag of 11.5 years in the introduction of foreign innovations into the Canadian smelting and refining industry, a lag of 9.1 years in respect of the electrical industrial equipment industry and 5.5 years in the case of telecommunications.[4]

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1. For a sample bibliography, see Appendix D.

2. Baldwin, J.R. and P.K. Gorecki, with J. McVey, "Canada-U.S. Productivity Differences in the Manufacturing Sector: 1970-1979", in McFetridge, D.G. (1986) Canada Industry in Transition (Toronto: Royal Commission on the Economic Union and Development Prospects for Canada).

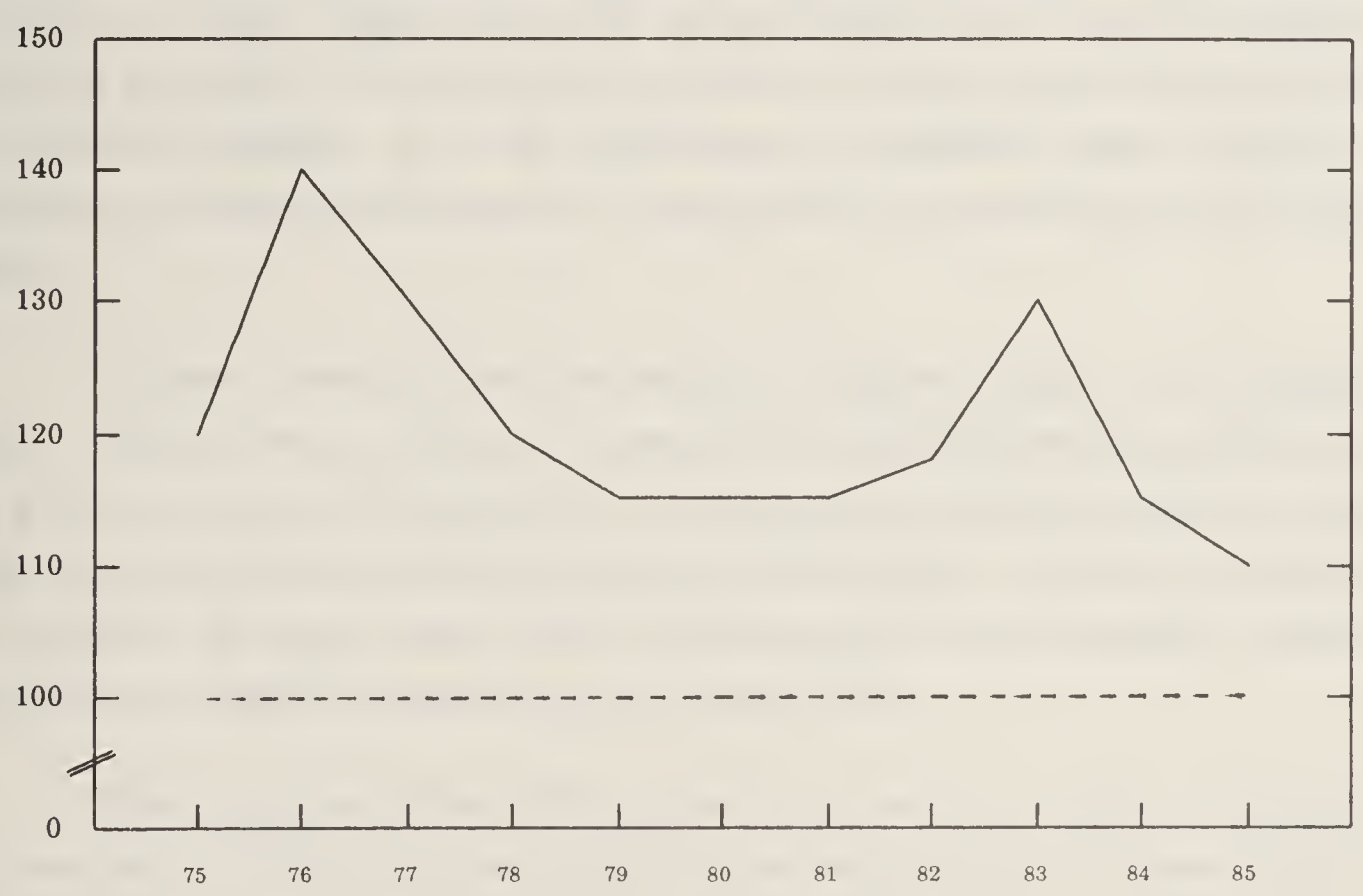
3. Canadian Trade in High Technology: An Analysis of Issues and Prospects, Ministry of State for Science and Technology, August 1985.

4. de Melto, D.P. et al., Preliminary Report: Innovation and Technological Change in Five Canadian Industries, Economic Council of Canada, 1980.

- High Debt/Equity Ratios. Canadian companies are more highly leveraged than their U.S. counterparts. In a number of industries, this structural feature has worsened over the past business cycle. For the future, high debt/equity ratios will make it more difficult for Canadian firms to finance the necessary adjustments to freer trade, especially those whose cash flows are reduced by loss of market share.

To ignore these competitive disadvantages of Canadian enterprise is to ignore an entire generation of scholarly effort. Yet, the argument remains that a bilateral trade agreement -- by expanding market opportunities and increasing competition in domestic markets -- may lead to industrial rationalization and productivity improvements in the long run. This is the essential "leap of faith". But a trade agreement should not be based on faith.

CANADA'S MANUFACTURING COMPETITIVENESS
(Canadian Unit Labour Costs as a % of US)



Source: Data Resources Incorporated.

It is true that Canadian manufacturing has substantially improved its competitive position with respect to U.S. manufacturing. Relative unit labour costs have come down from about 140 per cent of the American level in 1976 to about 110 per cent in 1985. However, our current competitiveness is largely a result of the depreciation of the Canadian dollar since 1976; it does not reflect underlying economic strength, or an ability to close the real income gap. In terms of a long term trade agreement, it is our productivity performance that will determine success. Otherwise, we are purchasing trade competitiveness at

the expense of continuing declines in our real income compared to Americans. It is Americans who gain, not Canadians, in such a situation.

In short, Canada's productivity record is grounds for caution about the potential positive effects of free trade. Canadian firms might not be able to exploit the opportunities, or withstand the competitive pressures, created by reduced tariff and non-tariff barriers. A comprehensive Canadian strategy is required to address the underlying dimensions of the productivity gap and improve Canada's trade prospects over the longer run. This is a national priority, with or without free trade.

The Auto Pact

The American negotiators may wish to buttress their arguments of benefits to Canada from open trade by referring to the current performance under the Auto Pact. The Auto Pact has been, on many counts, although not all, an important success. It is the centrepiece of Ontario's trade with the U.S. However, the Auto Pact stands as a model, not of free trade, but of managed trade.

In recent years, Canada has enjoyed a bilateral surplus in the automotive sector. This currently consists of a surplus on assembled vehicles of $10.6 billion and a deficit on parts of $5.9 billion. Excluding 1985, bilateral trade has been in rough balance over the years since the Auto Pact began. However, the data show that, despite the Auto Pact, relative productivity in the Canadian automotive sector did not improve significantly during the 1970s.

What happened after 1980 requires more careful analysis. The enormous improvement of Canadian productivity in the auto industry in recent years was not exclusively related to the absence of trade barriers under the Auto Pact. The fall in U.S. gasoline prices worked to Canada's advantage due to our specialization in vans and larger vehicles. In addition, the U.S. imposition of restraints on imports from Japan and the decline in the exchange rate both benefitted the competitive position of Canadian manufacturers. But these are not enduring advantages. To a large degree, they were events that few had anticipated. History could have worked differently, in which case the production safeguards, now easily surpassed, would have been critical. Indeed, it was only a few short years ago a disaster scenario was seriously considered for the Canadian industry.

The Auto Pact safeguards were undoubtedly essential for the protection of production and jobs in Canada as the North American industry rationalized its operations. They should be continued as an insurance policy on our future. The Auto Pact guarantees should not be on the negotiating table.

The Role of Multinational Corporations

Another unique feature of the Canadian, and Ontario, economies is the high degree of foreign ownership. Indeed, it is well beyond the degree of foreign ownership of United States industry. A substantial portion of Canada's output is produced in firms controlled by Americans.[4] For example, in 1981, U.S. residents controlled 63 per cent of Canada's value added in transportation equipment industries, 59 per cent of value added in the country's chemical industry, and over 45 per cent of value added in the electrical, petroleum, rubber and plastics, and machinery industries.

The significance of foreign control for the behaviour and performance of firms has been a subject of extensive academic study, both in Canada and abroad. One fact is clear. The corporate structure of multinational firms dictates behaviour which is often different from that of purely national enterprises.

Historically, the typical "truncated" branch plant was established to serve only the small Canadian market. Accordingly, U.S.-owned subsidiaries in Canada normally have a relatively low export orientation, especially when autos are excluded. Despite government encouragement, multinationals have not significantly rationalized their overall operations by granting global or North American product mandates to their Canadian subsidiaries. Generally, they have been precluded from competing with their parent in the U.S. and world markets. A survey of 800 foreign subsidiaries by Ontario's Ministry of Industry, Trade and Technology found that only a very small percentage of them had secured a global product mandate from their head office.

Foreign owned subsidiaries have very high import propensities compared to Canadian owned competitors. It is also widely documented that, in comparison to international standards, they have a low commitment to R&D.

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4. See Appendix C.

There are several issues in respect of foreign investment. The first is whether the behaviour patterns of foreign owned firms should be subject to public policy to encourage different responses. In this regard, Americans must appreciate the preponderance of such investment in Canada and its impact on our economic performance. If the collective performance of foreign owned firms is persistently unique and frustrates Canadian public policy goals, then it must be subject to corrective action. There is ample evidence that many Americans feel similarly about foreign investment in the U.S. This is despite the fact that foreign investment is miniscule in relation to total capital employed in the U.S.

It must also be recognized that the U.S. government displays a strong continuing interest in the activities of U.S. subsidiaries in other countries. This may well frustrate Canadian ability to meet both economic and social goals. The extraterritorial application of U.S. laws is a potentially serious problem for Canada, and must be thoroughly examined in any negotiations regarding U.S. investment in Canada.

Another issue relates to the response of multinationals given a free trade arrangement. Arguments have been made that an unconstrained movement to free trade could result in a liquidation of marginal branch plant investments in Canada.[5] Another possibility is that Canadian branch plants would not receive an equitable share of total corporate investment over the longer run, with the Canadian market being increasingly supplied from south of the border. There is evidence that a similar phenomenon has occurred within the U.S. as large corporations have gradually relocated to the U.S. South and Southwest.

A wide range of corporate responses to free trade might be expected since not all multinationals are structured in the same way. The uncertainty of these responses is important. Such considerations were held to be critical by the Government of Canada in 1965, when it insisted that production safeguards be included in the Auto Pact. They are no less valid today.

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5. For example, Baranson, Jack "Assessment of Likely Impact of a U.S.-Canadian Free Trade Agreement Upon the Behaviour of U.S. Industrial Subsidiaries in Canada". September, 1985.

The Service Sector

Since services account for about 70 per cent of total Canadian employment, particular attention will need to be focussed on enhancing productivity and competitiveness in this sector.

Canada's free trade vulnerability in respect of goods production stems largely from our fundamental productivity gap relative to the United States. That gap reflects, in part, the weakness of Canadian firms in achieving production economies in the plant, as well as corporate economies in marketing, R&D and finance. Many Canadian service industries, including some business and professional services, will experience similar, perhaps even greater, competitive problems relating to small firm size, marketing and access to capital. The importance to the service sector of intangible capital, such as previous professional or business association and goodwill, implies that access may be particularly difficult for exporters in this sector. Canada's large deficit in business services, which in 1985 totalled almost $2.3 billion, would seem to indicate considerable competitive disadvantages in this sector.

Trade in services, as well as in goods, is dependent on international flows of information. Transborder data flows and the corresponding information technologies constitute a significant and ever-changing force in the evolution of domestic economies and the international marketplace. As well, if information is power, then control of information is critical to sovereignty. In this regard, negotiations concerning extra-territorial application of law to the storage and transmission of data will be particularly important.

Services are an entirely new area of trade negotiation. However, the United States has clear objectives in respect of certain issues that impact primarily on service industries. The financial and insurance industries, for example, will become an important testing ground for the principles of "national treatment" and "right of establishment". Given the complexity of such principles, it would be preferable for Canada to negotiate service-related issues on an industry-by-industry basis.

Canada, through discussion with the provinces, needs to develop a full picture of the extent of regulation in the services field, along with a sense of which regulations are vitally necessary for the protection of consumer and corporate interests.

Transition and Adjustment

To the extent that gains from freer trade occur, they will entail rationalization of Canadian industry, involving new investment and worker retraining and relocation. Much of the adjustment would occur within individual industries, but some inter-sectoral shifts could be expected as well. The acceptability of free trade to Canadians will depend critically on how smoothly these adjustments can be brought about. This, in turn, is a function of the size of the adjustment expected under the basic agreement, the transitional measures embedded in it, and the labour and other adjustment policies independently put in place by governments on both sides of the border.

- The size of the adjustment "problem" is in part related to the anticipated gains in income from employment and investment shifts toward higher productivity industries. Those who expect large income gains must also accept that there will be large capital losses in certain sectors, significant investment requirements and large shifts in employment.

- Canadian industries are currently protected by higher tariffs than their U.S. counterparts and accordingly will face much greater adjustment requirements.

- The larger adjustment problem for Canadian industries also relates to Canada's greater trade dependency and the sizeable gap in Canadian relative productivity in certain areas. These factors suggest that Canada should pursue a long differential phase-in period, in which U.S. tariff and non-tariff barriers come down more rapidly than Canadian barriers.

- Adjustment assistance programs will be necessary even with differential phasing. These need to be secured as legitimate components of any free trade agreement.

- Canadian owned firms may be differentially affected. Canada should avoid agreeing to "national treatment" rules that preclude special transitional support directed to Canadian-owned firms.

- The behaviour of U.S. owned firms will also have to be addressed by overall safeguards.

CHAPTER IV. WHAT BENEFITS? AT WHAT COST?

It is important that U.S. negotiators appreciate that while the potential benefits to Canada are significant, they are not overwhelming. Moreover, whether these potential benefits are significant enough to produce an agreement depends critically on the U.S. realization that our existence as a nation requires that we maintain our ability to pursue independent social, economic and cultural goals.

Of course, no-one, certainly not the Americans, is suggesting that our collective goals, or our existence as a nation, are on the agenda for discussion. But what is on the agenda are the various policy tools that we use in our attempt to achieve these goals. Therefore, it is important that the U.S. not demand constraints on our policy instruments so great that they end up frustrating our national objectives in any case.

What Benefits?

Various attempts have been made to estimate the macroeconomic consequences of a free trade agreement. The results vary significantly, depending on the assumed features of the agreement, the start-up year (pre- versus post- Tokyo tariff levels), and the form of economic analysis adopted.

Some of the earlier and more general studies indicate real income gains to Canada in the order of 8 to 10 per cent. For example, Harris and Cox used a general equilibrium trade model to predict permanent real income gains in the order of 9 per cent, once all industry rationalization effects have occurred, and all productivity gains have been secured.[1]

More recent studies suggest much smaller gains. Harris, in a study for the Ontario Select Committee on Economic Affairs, takes account of obstacles to adjustment, and concludes that at the end of a ten year phase-in period, Ontario GPP under free trade would be only 1.69 percentage points higher than without it. Ontario's manufacturing sector would be the principal beneficiary. Also, consistent with the modest gains, adjustment problems would be minimal, at least over the period under review.

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1. Cox, David and Richard G. Harris, "A Quantitative Assessment of the Economic Impact on Canada of Sectoral Free Trade with the United States" December, 1984.

DIFFERENCE IN CUMULATIVE GROWTH IN ONTARIO AFTER TEN YEARS*
(Per Cent Change)

	GPP	Employment
Primary Industries	.291	-.273
Manufacturing Industries	3.057	.934
Transportation Equipment	3.177	.821
Services Industries	1.203	.088
Total Economy	1.690	.256

Source: R.G. Harris, "The Adjustment of the Ontario Economy to a Canada-U.S. Free Trade Arrangement", February 1986.

* Assumes 5-year phase-in to bilateral free trade by U.S., 10-year phase-in by Canada.

Work done by Informetrica Canada Ltd. suggests real output gains by the year 2005 of 2.4 per cent for Canada and 2.9 per cent for Ontario. Their study clearly shows Ontario as one of the largest gainers in the long run.

IMPACT OF "FULL ENHANCEMENT" RELATIVE TO BASE CASE

	Real Output Change (Per Cent)		Employment Change (000s)	
	1992	2005	1992	2005
Newfoundland	2.1	2.4	4	7
Prince Edward Island	2.1	3.1	1	2
Nova Scotia	1.6	2.4	3	8
New Brunswick	1.9	2.3	3	4
Quebec	1.4	2.1	13	29
Ontario	1.7	2.9	26	52
Manitoba	1.5	2.4	4	9
Saskatchewan	1.3	1.8	2	6
Alberta	1.1	1.5	4	11
British Columbia, Yukon and Northwest Territories	1.5	2.2	8	19
Canada	1.5	2.4	67	146

Source: Informetrica, "Economic Impacts of Enhanced Bilateral Trade: National and Provincial Results", 1985.

The prospect of achieving income and employment gains makes it worthwhile for Canada and the United States to explore options for improved trade. On the other hand, the estimated income gains in these models are not compellingly large especially given the long time frame before they are realized. The gains are also not large compared to other policy initiatives. For example,

during the recession of 1981-82, real output in Canada fell by 6.6 per cent. Had appropriate counter-cyclical policies reduced the severity of that recession by only half, or 3.3 per cent, the gain in output would be greater than that estimated for free trade.

At What Cost?

Free trade is an important economic initiative for Canada. However, it is a policy that does not address, nor is it meant to address, other important economic objectives. For example, there is no evidence that bilateral free trade will:

- diminish the severity of business cycles;
- promote the goal of regional development;
- increase the diversification of our industrial structure; and
- significantly improve Canada's employment prospects.

Therefore, it is important that U.S. negotiators appreciate that Canada cannot relinquish its freedom to pursue independent economic policies to achieve these other goals.

Cultural Industries

Canada is comprised of 25.5 million residents. The United States has 240 million. Canadians occupy the second largest nation in the world, with the longest coastline. About 90 per cent of the Canadian population is located within 100 miles of the U.S. border. These central facts, by themselves, would create problems of political sovereignty and integration. In Canada's case, there are further facts of regional economic differentiation, linguistic dualism and cultural pluralism.

Americans must appreciate that cultural policies are seen in Canada as essential vehicles of national unity. If, under freer trade, the economic orientation of Canada shifts further from East-West to North-South, cultural policy will become an even more important thread in the delicate fabric of Canadian identity and political independence.

Canadian producers of cultural products face commercial difficulties due to the small size of the Canadian market and its geographical segmentation. While Canada is fortunate to enjoy cultural diversity, this diversity further

fragments the size of the market and contributes to the problem of short production runs. Other problems for the domestically-controlled sector include restricted access to development capital, inadequate distribution and exhibition mechanisms, and the lack of marketing and financial expertise associated, in most cases, with small firm size.

Although Canadian products are often less profitable, there is also the possibility that the commercial potential of such products is underestimated by foreign-owned firms. Canadian cultural industries continue to suffer from this legacy. In a report for the Canadian Institute for Economic Policy (CIEP), Audley found that while markets for all cultural products are expanding in Canada, only a very limited percentage of content is of Canadian origin.[1] Foreign material in most sectors dominates domestic market shares. As well, the structure of the domestic production and distribution industries is typically organized around the supply of imported content to Canadians.

Trade flows tend to be skewed toward imports from the cultural metropolises, particularly the United States. The cultural sector runs a large balance of payments deficit. In printing and publishing alone, Canada had a $908 million trade deficit in 1985. Canada, in the early 1980s, was importing almost seven times as many books as it exported, four times as many TV programs and four times as many periodicals and newspapers.

The federal government and the provinces, recognizing the structural disadvantages of the cultural industries, have developed a number of programs to assist domestic entrepreneurs and artists. It is critical that Canada not relinquish its right, or its flexibility, to support its cultural industries. Such concessions by Canada will weaken our sense of national identity without offsetting benefits.

Regional Economic Development

Regional income disparities are significant in Canada. Personal income per capita in Canada's poorest province is only 68 per cent of the national average. Ten per cent of the Canadian population lives in provinces with personal income less than 80 per cent of the national average. Perhaps the most telling indicator of regional disparity is the unemployment rate. Currently, unemployment is running at 20.9 per cent in Newfoundland, 12.7 per cent in

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1. Audley, Paul Canada's Cultural Industries, James Lorimer and Company, Toronto, 1983.

British Columbia, 11.9 per cent in Quebec, around 8 per cent in the Prairies, and 6.8 per cent in Ontario.

Canada is comprised of a small population struggling to occupy a huge geographic land mass. Accordingly, the issues of regional development and regional income redistribution are perhaps more critical than they are in the United States. Significant out-migration from the less prosperous regions is not a feasible solution in Canada. There is, of course, substantial inter-regional migration, but the small size of the base population means that large scale out-migration can lead to virtual depopulation and substantial costs for those remaining. For example, a collapse of local housing markets could impose huge capital losses on everyone. Per capita taxes could rise to crushingly high levels to carry the overbuilt social infrastructure.

Canada's attack on regional disparity is, and must be, multi-faceted. Regional redistribution occurs indirectly through the income tax system and the way unemployment insurance operates. Direct development assistance is provided by the federal government through its expenditure and tax programs. For example, the Economic and Regional Development Agreements between the federal government and the provinces will finance about $4 billion in development expenditures over the next five years.

In addition, assistance is provided to provincial governments through equalization and shared cost programs. Equalization, currently running at about $5.3 billion a year, is in fact mandated by Article 36 of the recent Constitution Act. This program, more than any other, reflects the commitment by Canadians to providing a basic level of service, and a basic standard of living, to all residents wherever they may live in this country. It is not a new commitment, and it is one on which all governments in Canada are agreed.

Regional development and income redistribution inevitably involve costs which are borne by some Canadian taxpayers and some regions of Canada. As a consequence, where these policies might be seen to advantage some competitors, they clearly must disadvantage others in the same country. Americans must appreciate this reality, and respect the social and economic imperative of these policies.

Agricultural and Resources Policy

It is noteworthy that many of the trade irritants to the U.S. relate to Canadian practices in respect of resource industries -- for example, lumber, fish, hogs and potatoes. The resource industries are disproportionately important in less wealthy regions, and are an important element of their economic development. The pricing of resources, for example oil, gas and electricity, is often used as a regional development policy. To constrain this tool of development is to undermine what is often the only viable opportunity for growth.

Each country has a unique blend of geography and climate which profoundly influences economic development and government policies. For example, Canadian stumpage fees in part reflect the unavoidable facts that Canadian forests grow more slowly than forests in the Southern U.S., and are frequently less accessible to loggers. Similarly, in California, climate dictates the need for subsidized water. If the negotiators intend to develop a set of principles on "allowable" subsidies, they must start with a clear understanding of the circumstances that have led historically to the programs now in place.

Agriculture is, of course, a special case in both Canada and the United States:

- The cyclical nature of agricultural production, and the risks associated with weather, mean that North American agriculture faces greater uncertainty than most industrial sectors.

- Currently, the world over-supply of major agricultural commodities is negatively affecting prices received by North American farmers.

- Farming is a highly capital intensive industry. The high capital costs of land, buildings, and equipment, mean that those who have recently expanded capacity as well as new entrants have acquired heavy debt loads. These individuals are the hardest hit by low commodity prices and still burdensome real interest rates.

- Specialized soil and climatic conditions mean that there is, necessarily, regional specialization in farm production.

- Marketing systems in both Canada and the United States affect the level and stability of farm incomes. Over 20 per cent of Canadian farm cash receipts are related to supply-managed commodities (dairy, poultry, eggs and tobacco). There is both a high level of farm investment in the assets required to produce supply-managed commodities, and a significant gain to society from the income stability associated with these marketing systems.

Any attempt to change the rules relating to agricultural trade will unleash significant economic and social dislocation. Both Canada and the United States must recognize the current poor timing of a major bilateral trade initiative in this sector. However, general changes in contingent protection, as they affect agriculture, should be discussed.

Industrial Policy

The case for industrial policy is often based on the existence of market failures such as in the case of scientific research where social benefits exceed the private returns. In other cases, industrial subsidy is a defensive response to such subsidy by other countries. All countries resort to such policies. In Canada's case, there are other justifications as well.

International markets are rarely models of perfect competition. Many firms have market power and the ability to forestall competitors. Since Canadian firms are frequently small by international standards, they are disadvantaged in world markets. Industrial policy is a way to offset these disadvantages and make the "playing field" within any industry more equal.

Industrial policy can also be used to achieve a greater degree of economic stabilization through diversifying the industrial base. As conventional stabilization policies have become less and less relevant to an open economy such as Canada's, more emphasis has been placed on diversification of the industrial base to "build in" stabilizing features. The U.S. economy, on the other hand, remains amenable to macroeconomic management through monetary and fiscal policy.

Industrial policy takes different forms in different countries. In the United States, for example, industrial policy is closely linked to defence policy. The U.S. government has in recent years relied increasingly on defence expenditures as a tool of industrial and regional development. Federal funding of R&D performed for national defence accounted for more than 69 per cent of budgetted R&D in 1986. This figure has risen steadily since 1980 when the proportion was only 50 per cent. As a proportion of GNP, defence outlays accounted for 6.4 per cent in 1985, and will total 29.3 per cent of total 1986 budget outlays on all programs. In comparison, Canada allocated only 8.9 per cent of total budget expenditures to the Department of National Defence. These departmental outlays account for only 2.0 per cent of GNP.

A substantial and growing proportion of defense outlays are contracted to private industry in the U.S. Of all R&D obligations under the defence function, about 65 per cent are performed by private industry. Regionally, more than 20 per cent will be performed in the South Atlantic states. Defence contracting activities are heavily concentrated in low wage areas, as well as areas with substantial high tech industry. There is clearly a significant regional development factor evident in the distribution of these expenditures.

Canada has chosen to diversify its support for industrial development across a broad range of industries and sectors with a focus on commercial application and technology diffusion. It is a violation of the "level playing field" concept for Canada to be subject to countervail on subsidies when Canadian exporters are not able to contest equivalent subsidies provided through the U.S. defence establishment.

Stabilization Policy

The Canadian economy is extremely dependent on foreign trade. Consequently, business cycles tend to be imported. They are therefore less controllable by domestic macroeconomic policy tools.

In Canada's case, the availability of fiscal stimulus is further restricted by the existence of a federal deficit which, in relative terms, is larger even than the much-discussed U.S. federal deficit. As a result, Canada is forced to rely disproportionately on monetary and exchange rate policy for controlling the domestic economy. This dependency will grow under free trade as Canada's economy becomes increasingly integrated with that of the United States, and increasingly subject to business cycles emanating from that country.

The flexible exchange rate has been an important tool of adjustment for Canada. In recent years, flexibility in the exchange rate has facilitated necessary reductions in the real income of Canadians. It has done so by sharing the income loss more broadly and with less unemployment than would have been the case under a fixed rate. Fixed rates would have demanded even more deflationary domestic policies.

Yet many Americans regard the current Canada-U.S. exchange rate as a subsidy to Canadian industry. Much of the current U.S. trade deficit has been attributed to an "over valued" dollar. Indeed, the U.S. has recently achieved a substantial depreciation of its currency relative to several major competitors.

This has been achieved, in part, through agreement with those countries to encourage the depreciation. There is, however, no evidence to support a view that Canada's exchange rate is undervalued, or a deliberate subsidy to Canadian industry. Any attempt to "fix" the exchange rate between the two countries would eliminate for Canada a powerful tool of international and domestic adjustment. It would deprive us of our ultimate protection should free trade turn out to have a strongly negative effect on the Canadian economy. It would be a price too large.

Conclusion

It is vital that the U.S. negotiators recognize the significant structural differences between the U.S. and Canadian economies. These structural differences may well require the use of different policy instruments to pursue even mutually held goals. The "level playing field" has to take into account the unique characteristics of industrial structure, geography, climate, population and culture of our two countries.

APPENDIX A

ONTARIO'S MERCHANDISE TRADE
($ Million)

	Exports	Per Cent of Canada	Per Cent of GPP	Imports	Per Cent of Canada	Per Cent of GPP
1972	9,060	45	21	10,566	57	24
1976	15,660	41	21	20,344	54	27
1980	29,494	39	26	37,737	55	34
1984	55,202	49	34	59,576	62	37
1985	59,382	50	34	65,895	63	37

Source: Ontario Ministry of Industry, Trade and Technology and Statistics Canada.

ONTARIO'S MERCHANDISE EXPORTS TO THE U.S.: 1985
($ Million)

	1985	Per Cent of Total	Per Cent of Canada's Exports to U.S.
Food and Agricultural Products	1,299	2.4	34.3
Crude Materials	440	0.8	3.8
Fabricated Materials	11,798	21.9	41.0
Manufactured End Products	39,487	73.2	83.1
Special Transactions	855	1.6	79.4
TOTAL	53,909	99.9	58.0

Source: Ontario Ministry of Industry, Trade and Technology and Statistics Canada.

CANADA'S CURRENT ACCOUNT WITH THE U.S. AND CURRENT ACCOUNT BALANCE WITH ALL COUNTRIES: 1985
($ Millions Cdn.)

Item	Exports (Receipts)	Imports (Payments)	Canada-U.S. Balance	Canada-All Countries Balance
Merchandise[1]	94,656	74,119	+20,537	+16,817
Services[2]	11,161	24,721	-13,560	-20,503
Sub-Total				
Goods and Services[2]	105,817	98,839	+6,977	-3,686
Transfers	580	424	+155	+1,038
Total Current[3]	106,396	99,263	+7,133	-2,648

Source: Statistics Canada, Cat. No. 67-001P, Preliminary Estimates February 28, 1986.

1. Merchandise trade flows are in balance of payments basis.
2. Services include interest and dividends.
3. Totals may not sum due to rounding.

CANADA'S SERVICE TRADE COMPONENTS WITH THE U.S.: 1985
($ Millions Cdn.)

	Exports (Receipts)	Imports (Payments)	Balance
Travel	3,633	4,141	-508
Interest and Dividends	1,121	8,621	-7,500
Freight and Shipping	2,433	2,645	-213
Other Services	3,975	9,313	-5,339
- Government Transactions	244	474	-230
- Miscellaneous Income	971	3,803	-2,832
- Business Services and Other Transactions	2,760	5,037	-2,277
Total Services	11,161	24,721	-13,560

Source: Statistics Canada, Cat. No. 67-001P, Preliminary Estimates February 28, 1986.
Note: Totals may not add due to rounding.

APPENDIX B

REAL DOMESTIC PRODUCT, BY PROVINCE AND INDUSTRY: 1984
(Per cent of each province's total GDP)

	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.
Agriculture	0.4	9.4	1.4	1.3	1.4	2.0	4.8	11.6	4.3	1.5
Forestry	1.0	0.0	0.4	1.5	0.6	0.3	0.1	0.2	0.1	2.8
Fishing	1.6	2.3	1.4	0.5	0.0	0.0	0.1	0.0	0.0	0.2
Mining	8.2	0.0	2.8	2.7	0.7	1.0	2.2	7.7	11.1	2.7
Manufacturing	7.6	7.9	13.3	15.6	23.6	29.3	13.9	5.7	8.3	13.9
Construction	8.5	4.8	7.4	7.0	4.3	3.8	2.1	6.8	6.9	5.1
Utilities	10.3	1.8	2.9	4.4	4.6	2.9	3.9	3.8	3.1	3.3
Goods-Producing Industries	37.6	26.5	29.7	33.0	35.2	39.3	27.0	35.6	33.8	29.6
Transportation and Communication	11.3	8.1	11.5	13.1	9.1	7.8	17.1	17.9	14.6	17.1
Wholesale and Retail Trade	12.5	14.5	13.2	13.0	14.1	12.8	14.7	12.1	12.5	12.5
Finance, Insurance and Real Estate	8.8	10.4	12.6	11.3	13.8	13.3	15.4	11.9	14.7	14.3
Community, Business and Personal Service	17.8	20.6	13.9	11.4	6.6	6.2	7.6	6.2	6.8	6.9
Public Administration and Defence	12.0	20.1	13.9	11.4	6.6	6.2	7.6	6.2	6.8	6.9
Service-Producing Industries	62.4	73.5	70.3	67.0	64.8	60.7	73.0	64.4	66.2	70.4

Source: Conference Board of Canada Estimates.

REAL DOMESTIC PRODUCT, BY PROVINCE AND INDUSTRY: 1984
(Provincial percentage of industry total)

	Nfld.	P.E.I.	N.S.	N.B.	Que.	Ont.	Man.	Sask.	Alta.	B.C.
Agriculture	0.2	1.2	1.5	1.1	13.2	31.6	7.5	17.6	19.2	6.9
Forestry	2.0	0.0	1.8	4.4	21.1	18.1	0.6	1.1	1.9	20.8
Fishing	17.6	5.7	30.8	8.2	6.3	5.0	3.1	0.6	2.0	48.9
Mining	4.2	0.0	2.8	2.0	6.0	14.8	3.1	10.6	44.9	11.7
Manufacturing	0.5	0.1	1.7	1.5	25.4	55.3	2.6	1.0	4.3	7.6
Construction	2.5	0.3	4.3	3.0	20.8	32.4	1.8	5.5	16.5	12.8
Utilities	4.1	0.2	2.2	2.5	29.7	32.5	4.3	4.1	9.7	10.8
Goods-Producing Industries	1.5	0.2	2.2	2.5	22.7	44.3	3.0	3.8	10.6	9.7
Transportation and Communication	1.4	0.2	2.9	2.4	19.0	28.6	6.2	6.2	14.8	18.2
Wholesale and Retail Trade	1.3	0.3	2.8	2.0	24.6	39.3	4.4	3.5	10.6	11.1
Finance, Insurance and Real Estate	0.9	0.2	2.5	1.7	23.2	39.2	4.5	3.3	12.0	12.3
Community, Business and Personal Service	1.3	0.3	2.6	1.8	24.3	41.6	3.6	3.1	9.9	11.4
Public Administration and Defence	2.4	0.9	5.5	3.3	21.6	35.9	4.3	3.4	11.0	11.6
Service-Producing Industries	1.4	0.4	3.0	2.1	23.0	37.8	4.5	3.8	11.4	12.7

Source: Conference Board of Canada Estimates.

APPENDIX C

U.S. CONTROL OF CANADIAN INDUSTRY: 1970 AND 1981
(Per Cent)

Industry	U.S. Control of:					
	Shipments		Value Added		Employees	
	1970	1981	1970	1981	1970	1981
All Manufacturing	42	36	43	34	36	29
Food and Beverage	24	20	28	26	24	20
Rubber and Plastics	68	50	68	52	61	45
Textiles	39	39	42	41	32	31
Clothing	x	13	x	14	x	12
Wood	22	16	20	15	19	13
Furniture and Fixtures	16	13	17	15	16	12
Paper and Allied	35	22	35	22	34	20
Printing and Publishing	8	7	8	8	6	7
Primary Metals	38	8	40	7	38	8
Metal Fabricating	34	29	33	30	29	25
Machinery	64	45	72	47	63	43
Transportation Equipment	83	74	78	63	70	58
Electrical Products	55	45	56	48	55	49
Non-Metallic Mineral Products	26	23	25	24	24	24
Petroleum and Coal Products	68	56	73	56	70	62
Chemicals and Chemical Products	62	58	64	59	56	54
Miscellaneous Manufacturing	x	36	x	41	x	33

Source: Statistics Canada, Cat. No. 31-401.
Note: x - Confidential to meet secrecy requirements of the Statistics Act.

CAPITAL EMPLOYED IN CANADIAN NON-FINANCIAL INDUSTRIES CONTROLLED BY U.S. RESIDENTS: 1974-1984
(Per Cent)

	1974	1978	1981	1984
Manufacturing	43	41	39	38
Petroleum and Natural Gas	59	41	36	35
Mining and Smelting	45	38	30	27
Railways	2	1	1	1
Other Utilities	4	4	3	3
Total, Above Industries and Merchandising	26	22	20	20

Source: Statistics Canada, Cat. No. 67-202, and Balance of Payments Division (for 1981 and 1984).

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